NNSA
Business Management Advisory Council
White Paper
Tolerances in Accounts Payable

Several working groups were created as spin-offs of the NNSA sponsored Hackett benchmarking study, Accounts Payable among them, which were chartered to investigate the differences in statistics between the sites, normalize the data if necessary, and determine whether there were areas of opportunity for cost savings and/or efficiencies. The Accounts Payable working group rapidly determined that the apparent differences between the sites were primarily due to interpretation of the data requested. After normalizing the data, one significant opportunity was evident.

The government [DOE] is generally risk averse and that attitude is transferred to the M&O contractors that operate the various sites on behalf of DOE. Consequences drive behavior and when the consequence is unallowable cost, the behavior is to take whatever steps are necessary to reduce or eliminate the unallowable cost. In this case, the behavior is to set the system to zero tolerance and to require all purchase orders (PO) be officially modified by Procurement before payment can be made for the additional items.

An easy example is Xerox paper. Suppose a PO is written for 100 cases of paper at $50 per case for a total of $5000. And suppose 105 cases are actually delivered. There is a cost associated with returning the extra 5 cases. In addition, we know that the extra 5 cases would be utilized by the operation in the near future. In the commercial world, the tolerance would be applied and the vendor simply paid for the additional 5 cases. In a zero tolerance government world, the purchase order would be sent back to Procurement for the additional 5 cases with the appropriate dollars to be added to the commitment. This takes time and effort which costs money.

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There is a "cost of doing business" associated with the operation of any facility, whether it be a government laboratory, a production facility or a commercial/private enterprise. Government requirements tend to make that cost greater than private industry; however, it should be a goal within government to drive the cost of operations down closer to commercial standards. To require that purchasing documents be revised for small excess quantities when the commercial world does not do so appears to be an area in which government operations could improve.

Hackett does not normally collect information in this area; however, they did provide some statistics which indicate that the lower bound for revising purchase orders in the commercial world is $1000. In checking with some of our parent companies and affiliates, a commonly used tolerance is the lesser of 5% or $1000. This provides a built-in internal control against abuse and excessive risk.

It will not benefit the integrated contractors if they each set tolerances which are not ultimately accepted by auditors (whether Internal Audit, the IG, OFFM reviews, etc). If audit determines that payment over the precise amount committed is an audit finding, that will drive the integrated contractors back to zero tolerances. It needs to be made clear to all auditors that payments made in accordance with whatever level of tolerance is acceptable to DOE are not audit findings and are allowable cost.

We recommend that NNSA issue an official document accepting any tolerances in Accounts Payable up to the lesser of 5% or $1000.